

# ANALYSIS OF ORIGINAL BILL

## Franchise Tax Board

Author: Harman Analyst: LuAnna Hass Bill Number: AB 2530  
Related Bills: See Legislative History Telephone: 845-7478 Introduced Date: February 21, 2002  
Attorney: Patrick Kusiak Sponsor: Personal Insurance Federation

**SUBJECT:** Disclosure Of Return Information In Proceeding Involving An Allegation Of Loss Of Earnings

### SUMMARY

This bill would broaden the type of judicial or administrative proceeding in which tax return information could be disclosed.

### PURPOSE OF THE BILL

According to the bill's sponsor, the Personal Insurance Federation Corporation, the purpose of this bill is to allow tax returns to be admissible in proceedings regarding insurance coverage and a taxpayer's allegation of a loss of earnings.

### EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative January 1, 2003.

### POSITION

Pending.

### ANALYSIS

#### FEDERAL/STATE LAW

Existing federal and state law prohibits the disclosure of any taxpayer information, except as specifically authorized by statute. In addition, state tax law provides that information collected on income tax returns is considered confidential and, unless specifically required to be available for other uses, shall be used only to administer the income tax laws.

#### Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
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<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

#### Department Director

#### Date

Gerald H. Goldberg

04/08/2002

Under state law, a tax return or the information on a tax return may be disclosed in a judicial or administrative proceeding regarding tax administration. In order for the information to be disclosed in such a proceeding, specific criteria must be met.

- The taxpayer must be a party to the proceeding, or the proceeding must have come about, or is in connection with:
  - determining the taxpayer's civil or criminal liability regarding any income or corporation tax, or
  - the collection of the taxpayer's civil liability regarding any income or corporation tax.
- The treatment of an item reflected on the return is directly related to the resolution of an issue in the proceeding.
- The tax return or the information on the tax return directly relates to a transactional relationship between a person who is a party to the proceeding and the taxpayer, which directly affects the resolution of an issue in the proceeding.

State income tax law allows the Franchise Tax Board (FTB) to charge a fee for providing persons with copies of their tax returns. The fee includes the costs of handling requests, copying documents, and postage. In addition, FTB may charge for the reasonable costs of its services whenever FTB is required or permitted to disclose information to any official, department, bureau, or agency of California, any other state, or the United States.

### THIS BILL

This bill would allow a tax return or the information on a tax return to be disclosed in a judicial or administrative hearing involving any allegation of loss of earnings or earning capacity by the taxpayer.

### IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns.

As stated above under "State Law," specific criteria must be met in order for return or return information to be disclosed. The criteria have a meaning specific to the context of proceedings "pertaining to tax administration." This bill would create ambiguity in attempting to apply existing criteria used to determine if confidential taxpayer information should be disclosed for purposes of tax administration and apply those criteria to a judicial or administrative proceeding involving an allegation of loss of earnings or earning capacity. The author may wish to create separate specific criteria outlining when return information should be disclosed in this type of proceeding.

Currently, FTB is permitted to charge taxpayers a fee or charge other governmental agencies for the reasonable costs of disclosing information. A third party other than the taxpayer or another state agency could initiate the proceedings regarding an allegation of loss of earnings. This bill lacks a provision that would allow FTB to charge the third party for the costs of disclosing information. Therefore, it is unclear who would be responsible for the costs of disclosing information.

## OTHER STATES' INFORMATION

A review of *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York* laws found that *Florida, Illinois, Massachusetts, Minnesota, and New York* have income tax disclosure laws similar to California's current income tax disclosure laws. *Michigan* law states that disclosure may be allowed to a third party pursuant to a judicial order if the disclosure is to other agencies investigating:

- support obligations in domestic relations matters,
- criminal matters, and
- whether a taxpayer's tax liability is to be adjudicated.

The laws of these states were reviewed because their tax laws are similar to California's income tax laws.

## FISCAL IMPACT

It is anticipated that this bill could result in a significant increase in the number of subpoenas for records served on the department. The department's responses to the subpoenas would substantially increase the amount of staff time spent to review and determine whether records were releasable. In addition, staff would be required to assemble, track, and send out the documents requested. Depending on whether the subpoena required the personal appearance of a custodian of records, the department could incur costs for the additional hours in personal appearances. The additional costs have not been determined at this time. If this bill continues to move through the legislative process, costs will be identified and an appropriation will be requested.

## ECONOMIC IMPACT

This bill would not impact the state's income tax revenue.

## ARGUMENTS/POLICY CONCERNS

Consistent with the general statutory bias against disclosure of tax returns or tax return information, current law allows use of tax returns or return information in relatively few proceedings, primarily those involving tax administration such as criminal prosecutions or civil suits for tax refund. This bill would allow disclosure whenever a claim of lost earnings or earning capacity is *alleged*, which could substantially expand the judicial or administrative proceedings in which tax returns or return information could be lawfully subpoenaed and thus made public. Many, if not most, of the common civil actions for personal injury (most of which contain a claim for lost earnings or earnings capacity) could result in subpoenas for tax return information.

As stated above under "Purpose of the Bill," the intent of this bill is to allow tax returns to be admissible in a proceeding involving an insurance company and a taxpayer's allegation of loss of earnings. In *Webb v Standard Oil Co.* (1957) 49 C.2d 509, an insurance company defendant was prohibited from using tax return information to impeach the testimony of the plaintiff/taxpayer. Specifically, the court wrote that the wording of Revenue and Taxation Code Section 19545 (previously 19283) discloses an intent to preserve the secrecy of the returns except in the few situations that are expressly noted within the provision. This bill would conflict with the underlying rationale for the court's decision, which is to encourage accurate reporting of income and deductions in a self-assessing tax system.

Historically, information privacy in general has been the topic of heated debate. This bill would expand the circumstances in which taxpayer information can be disclosed, which would hinder the department's ability to keep taxpayer information private and may compromise the integrity of the self-assessed tax system. Further, California's voluntary compliance tax system relies on taxpayers accurately reporting their income. If taxpayers perceive that tax information may be easily shared or otherwise compromised, the voluntary compliance system may be jeopardized.

#### **LEGISLATIVE STAFF CONTACT**

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